Supreme Court, U.S.
FILED
JUN 1 1998
CLERK

No. 96-1570

IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

NYNEX CORPORATION,
NYNEX MATERIEL ENTERPRISES COMPANY,
and NEW YORK TELEPHONE COMPANY,
Petitioners,

v.

DISCON, INCORPORATED,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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BRIEF FOR PETITIONERS

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QUESTIONS PRESENTED

When a Purchaser agrees to buy from Supplier A rather than Supplier B, and there is no issue of any horizontal restraints or vertical price restraints:

1. May the agreement between Purchaser and Supplier A be characterized as a group boycott in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1?

2. May the agreement between Purchaser and Supplier A be characterized as a conspiracy to monopolize in violation of Section 2 of the Sherman Act, 15 U.S.C. § 2?

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BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-20a) is reported at 93 F.3d 1055. The opinion of the district court dismissing the amended complaint (Pet. App. 21a-53a) is not reported. The opinion of the district court dismissing the original complaint (J.A. 42-72) is not reported.

JURISDICTION

The judgment of the court of appeals was entered on August 26, 1996. Pet. App. 1a; J.A. 124-25. A petition for rehearing, with a suggestion for rehearing en banc, was denied on January 7, 1997. Pet. App. 54a-55a. The petition for writ of certiorari was filed on April 4, 1997. This Court has jurisdiction under 28 U.S.C. §§ 1254(1)

and 2101(c). The Court granted the petition for a writ of certiorari on March 23, 1998. J.A. 126.

STATUTES INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, provides in pertinent part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal.

Section 2 of the Sherman Act, 15 U.S.C. § 2, provides in pertinent part:

> Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony * * *.

STATEMENT

Respondent Discon, Incorporated, was a supplier to telephone companies of removal services, *i.e.*, "the salvage and disposal of obsolete telephone central office equipment." J.A. 78 (Amended Complaint ¶ 13). Petitioner NYNEX Corporation was the parent corporation of petitioner New York Telephone Company (NYT), which provided regulated telephone service in New York, and of petitioner NYNEX Materiel Enterprises Company (MECo), a subsidiary that acted as a purchasing agent for NYNEX and its affiliates.[1] For two years in the mid-

[1] Except where relevant to distinguish among them, petitioners are referred to collectively as NYNEX.

The information required by Rule 29.6 of this Court's Rules, concerning parent companies and nonwholly owned subsidiaries, is set forth at Pet. ii-iii, supplemented by the fact that NYNEX Corporation is now a subsidiary of Bell Atlantic Corporation. All the current parties to the proceeding are listed in the caption. Two additional named defendants, Robert Eckenrode and Bernard O'Reilly, were not named in the Sherman Act counts at issue in this Court; all of the counts naming them have been dismissed.

1980s, Discon sold removal services to NYNEX, either directly to NYT or through MECo. Several years after NYNEX stopped buying removal services from it, Discon sued for treble damages under the Sherman Act, 15 U.S.C. §§ 1, 2, 15. The Second Circuit held that Discon had stated two valid antitrust claims, for conspiracy in restraint of trade and conspiracy to monopolize.

NYNEX challenges that ruling. The Second Circuit relied on inapplicable categories of antitrust law and mistreated as an antitrust problem what is at most an alleged fraudulent evasion of other regulatory regimes governing rates in the telephone-services market, which is not even alleged as a relevant antitrust market here. In so doing, the court authorized costly antitrust litigation over a firm's replacement of one of its suppliers even though there are no specific and plausible allegations of any harm to competition (as opposed to harm to Discon alone) in the removal-services markets actually alleged.

A. Background

In 1990, Discon filed a 16-count complaint including claims of conspiracy to restrain trade, monopolization, attempted monopolization, and conspiracy to monopolize. J.A. 3-41.[2] After the district court dismissed the complaint with leave to replead, Discon filed an amended complaint. J.A. 42-72, 73-123. Because the issue before this Court is whether the amended complaint was properly dismissed, the allegations in that complaint are assumed to be true.

The antitrust claims at issue do not involve any market in which NYNEX is a seller of telephone services to consumers. Rather, they involve a single product, namely, removal services, sold by Discon in two alleged markets—"the markets for removal services [1] at NYT and [2] in

[2] Discon also presented claims under the Racketeer Influenced and Corrupt Organizations (RICO) Act, 18 U.S.C. § 1962, and numerous state-law claims. All of the non-antitrust claims have been dismissed and are no longer in the case.

the New York State area." J.A. 112 (Am. Compl. ¶ 107, conspiracy to monopolize); J.A. 112 (Am. Compl. ¶ 110, conspiracy to restrain trade) (bracketed numbers added).[3] AT&T was allegedly "the dominant supplier of removal services in New York State." J.A. 82 (Am. Compl. ¶ 26). At the same time, according to Discon, AT&T and NYNEX, as telephone companies, were the "only major *purchasers* of removal services in New York State." J.A. 76 (Am. Compl. ¶ 2) (emphasis added); *see* J.A. 83 (Am. Compl. ¶ 29). *See also* J.A. 111 (Am. Compl. ¶ 104) (NYNEX "effectively controlled the price at which contracts for removal services were obtained").

Beginning in 1984 and until mid-1986, NYNEX bought some removal services from the newly formed Discon—specifically, NYT bought the services either directly or through MECo, the NYNEX purchasing agent—while also buying such services from AT&T. *See* J.A. 87-90 (Am. Compl. ¶¶ 40-52). Many telephone companies, including NYNEX, rather than buying all of their removal services from outside sellers, used their own employees for much of this kind of dismantling and disposal work. J.A. 83 (Am. Compl. ¶ 27). Even while using Discon, NYNEX assigned AT&T "supervisory and quality control responsibilities" for at least some of the Discon projects. J.A. 85-86 (Am. Compl. ¶¶ 33, 36).

In 1986, NYNEX stopped buying from Discon. J.A. 91 (Am. Compl. ¶¶ 53, 55). The amended complaint itself identifies a basis for the termination (which has been denied by Discon): improper conduct by Discon. In particular, NYNEX learned that Discon had lent money to a NYNEX contracting officer without expectation of

[3] The definition of the relevant product markets as markets for removal services purchased by telephone companies like NYNEX is repeated throughout the amended complaint, including in all of the antitrust claims. *See, e.g.*, J.A. 75-76 (Am. Compl. ¶¶ 1-3), 80 (Am. Compl. ¶ 20), 82, 83 (Am. Compl. ¶ 29), 84 (Am. Compl. ¶¶ 32-33), 91 (Am. Compl. ¶ 55), 110 (Am. Compl. ¶¶ 98-99, attempt to monopolize), 111 (Am. Compl. ¶ 104, monopolization).

repayment, then hired that contracting officer once he left NYNEX. *See* J.A. 85, 90-91, 121-22 (Am. Compl. ¶¶ 33(a), 50, 53, 165-66).

Discon, however, alleged that its termination as a supplier to NYNEX was the result of a conspiracy between NYNEX and AT&T, which the amended complaint—while alleging no more than an agreement that NYNEX would buy from AT&T rather than Discon—characterizes as an agreement to "discriminate against Discon" and "to exclude Discon from the market." J.A. 84 (Am. Compl. ¶¶ 33, 31). As a result of its termination, Discon alleged, NYNEX "agreed to award [AT&T] *most* contracts on a non-competitive basis" (J.A. 84 (Am. Compl. ¶ 31)) and to "award *virtually all* its contracts" for removal services to AT&T (J.A. 112, Am. Compl. ¶ 110). (Emphases added.) *Cf.* J.A. 76 (Am. Compl. ¶ 3 (NYNEX "awarded contracts to AT&T on a preferential or exclusive basis")). In this Court, Discon has characterized its amended complaint, not as alleging a full "requirements" contract or other exclusive-dealing contract between NYNEX and AT&T, but as alleging that AT&T provided "the lion's share" of removals needed by NYNEX. Br. in Opp. 5.[4]

Although the amended complaint alleges harm to Discon as an individual competitor,[5] it contains no allegations

[4] Discon did not name AT&T as a defendant in this case. (Although the amended complaint distinguishes AT&T Technologies, which provided removal services, from AT&T Communications, which sold long-distance telephone service, the two companies are properly treated as the single entity, AT&T.) A separate lawsuit by Discon against AT&T was dismissed with leave to replead, but Discon did not replead or appeal. Decision and Order, *Discon, Inc. v. AT&T Technologies*, No. 90-545A (W.D.N.Y. June 25, 1992).

Discon's claim of a Section 2 conspiracy to monopolize also alleges two other conspirators, LISN (a seller of removal services) and Robert McGee, a subcontractor in Buffalo. *See* J.A. 111-12 (Am. Compl. ¶ 107), 85 (Am. Compl. ¶ 33(a)).

[5] Discon's termination as a supplier to NYNEX allegedly "restrained Discon from competing in markets for removal services

about exclusion of other competitors selling removal services, about any resulting constriction of supply that harmed the buyers in the markets for removal services (*i.e.*, telephone companies), or about barriers to new entry into this business. Significantly, in light of what is thus *not* alleged, the amended complaint itself refers to other present and potential suppliers of removal services (J.A. 111 (Am. Compl. ¶ 107) and notes that telephone companies often use their own employees to do this work (J.A. 83 (Am. Compl. ¶ 27)). Moreover, Discon's original complaint details Discon's own quick entry and rapid expansion: Discon was formed in June 1984, won a $500,000 contract in its first month, and, within only six months, had 25 employees and was planning to hire 50 more. J.A. 15, 17 (Compl. ¶¶ 50, 52, 61); *see* J.A. 87 (Am. Compl. ¶ 40, 1984 contract).

The amended complaint explains the alleged NYNEX-AT&T agreement to replace Discon as a supplier to NYNEX, not in familiar antitrust terms as an effort driven by Discon's competitor (AT&T), but rather as a scheme undertaken by NYNEX to engage in regulatory fraud as a seller of telephone services. According to Discon, the goal of the purported agreement was to enable NYNEX to evade regulatory limits on its rates in the distinct market for telephone services sold by NYNEX (specifically, NYT) under cost-of-service regulation imposed by the New York Public Service Commission and Federal Communications Commission. J.A. 76, 83, 93-94 (Am. Compl. ¶¶ 2, 29, 64). In particular, NYNEX allegedly agreed to buy removal services from AT&T at artificially high prices,

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and injured it in its business." J.A. 91 (Am. Compl. ¶ 55). *See* J.A. 92, 112-13 (Am. Compl. ¶¶ 58, 108, 113). The amended complaint does not indicate why termination of Discon as a supplier to NYNEX prevented it from selling removal services elsewhere. *See* J.A. 91 (Am. Compl. ¶ 53, proposed work for BellSouth). Discon's home base in Buffalo is no closer to New York City, which is within the alleged markets, than to various points (*e.g.*, in Ohio, Pennsylvania, Rochester, etc.) served by telephone companies other than NYNEX.

which were then incorporated into the cost basis for setting telephone-service rates, thus fooling the state and federal regulators into allowing inflated telephone rates; later, NYNEX allegedly received a secret rebate from AT&T to reduce the initially excessive price for removal services. *Id.*[6] Allegations that NYNEX had made excessive payments for certain equipment and services purchased through its MECo subsidiary, and thereby secured inflated regulatory rates, were the specific subject of federal and state regulatory proceedings, although no findings were made either that NYNEX had committed fraud or that NYNEX had improperly used AT&T rather than Discon for its removal services.[7] The amended complaint alleges that the regulators' rate adjustments were inadequate to compensate Discon and other ratepayers. J.A. 94-95 (Am. Compl. ¶¶ 68, 70).[8]

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[6] The amended complaint alleges that excess prices were paid both on direct purchases by NYT and on purchases made through MECo. J.A. 84, 93-96 (Am. Compl. ¶¶ 31, 64-73). As the Solicitor General has pointed out, the amended complaint does not explain the relationship between the alleged scheme to defraud regulators through excessive prices and Discon's alleged exclusion from the removal-services business. *See* Brief for the United States and FTC on Petition for Certiorari at 8 n.4 (hereafter SG Pet. Br.).

[7] *See New York Telephone Co.*, 5 F.C.C.R. 866 (1990) (initiating enforcement action for alleged "unreasonable markups and overcharges by MECO"); 5 F.C.C.R. 5892 (1990) (settlement of proceeding by payment of refund); *New York Telephone Co.*, 31 N.Y.P.S.C. 485, 511-13 (1991), *aff'd sub nom. New York Telephone Co. v. Public Service Comm'n*, 190 A.D.2d 217, 597 N.Y.S.2d 760 (3d Dep't 1993).

Whether an unregulated affiliate is limited to the regulated utility's prescribed rate of return has been a recurrent regulatory issue (*see* 5 F.C.C.R. at 867-68), and whether particular expenditures are reasonable is an issue endemic to traditional rate-of-return utility regulation (*see* 190 A.D.2d at 220-24, 597 N.Y.S.2d at 761-63). Rejection of a utility's position in either regard does not imply fraud on the utility's part.

[8] In addition to suing as a competitor in the removal-services markets, Discon sued as a ratepayer buying telephone service from

Based on those allegations, Discon claimed that NYNEX and AT&T violated Section 1 by agreeing "to fix prices and to restrict competition in the markets for removal services at NYT and in the New York State area." J.A. 112 (Am. Compl. ¶ 110). Discon also made three claims under Section 2 of the Sherman Act—which are comprehensible only on Discon's theory that NYNEX's wholly owned subsidiary MECo, which acted as a purchasing agent and did not provide any removal services of its own, was a separate entity acting as a supplier of removal services in competition with Discon.[9] Discon alleged that the NYNEX companies had "attempted to monopolize" the removal-services markets (J.A. 110 (Am. Compl. ¶ 100)) and had succeeded in monopolizing the removal-services markets (J.A. 111 (Am. Compl. ¶ 104)) and, also, that the NYNEX companies "combined and conspired with others, including [AT&T and two other removal-services providers], with the specific intent to violate Section 2 of the Sherman Act by monopolizing" the same markets. J.A. 111-12 (Am. Compl. ¶ 107). The amended

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NYNEX (*e.g.*, J.A. 77, 113 (Am. Compl. ¶¶ 3, 113)), but the district court dismissed those claims as barred by the filed rate doctrine (Pet. App. 32a), and Discon did not appeal that ruling. The amended complaint also makes reference to NYNEX's purchase of certain computer and other equipment (*e.g.*, J.A. 76, 92 (Am. Compl. ¶¶ 2, 59)), but the counts stating the antitrust claims (J.A. 110-113 (Am. Compl. ¶¶ 97-113)) do not involve markets for such equipment, which do not appear to have anything to do with Discon. The case, accordingly, is only about the alleged markets for removal services.

[9] MECo, a wholly owned subsidiary of NYNEX, acted only as a *purchasing* agent for the NYNEX companies (*see, e.g.*, J.A. 79 (Am. Compl. ¶ 16)), and "[i]t is undisputed that MECo itself [did] not perform any removal services for NYTel" (Pet. App. 8a). As the Solicitor General has acknowledged, in agreement with the Second Circuit (Pet. App. 8a-10a), the various NYNEX petitioners are properly treated as a single entity. *See* SG Pet. Br. 2 n.1.

complaint seeks damages that "exceed $75 million." J.A. 123 (Am. Compl. ¶ 173).

B. The Court of Appeals Decision

After the district court dismissed the amended complaint (Pet. App. 21a-52a), the Second Circuit reversed. Pet. App. 1a-20a. The court of appeals agreed with most of the district court's rulings, including its dismissal of the claims of monopolization and attempted monopolization. Pet. App. 15a-20a. Nevertheless, relying on new theories not presented by Discon, the court of appeals reinstated the amended complaint's claims of Section 1 conspiracy and Section 2 conspiracy.

As to Section 1, the court of appeals first held that the district court had correctly rejected Discon's attempt to characterize its allegations of a NYNEX-AT&T agreement as involving a *horizontal* agreement. It explained that MECo was wholly owned by and acted only as a purchasing agent for NYNEX, so that the NYNEX companies were properly treated as a single entity that was only a purchaser of removal services from Discon and AT&T, not a competitor of Discon and AT&T in the market for the sale of such services. Pet. App. 8a-10a (rejecting characterization of MECo as distinct from NYNEX, relying on *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984) (corporate family treated as single entity for antitrust purposes)). Having established that the alleged agreement is only a *vertical* one, the court of appeals next rejected Discon's attempt to characterize the agreement as one to fix prices under this Court's *per se* rule against vertical agreements to set minimum resale prices (*see Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 724 (1988)). Pet. App. 10a n.5.[10]

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[10] Removal services were not to be resold by NYNEX at all. In its brief in opposition to the petition for certiorari, Discon did not dispute the Second Circuit's rejection of its "theory of vertical price-fixing" (Pet. App. 10a n.5).

The court of appeals nevertheless ruled that "Discon may be able to prevail under a different legal theory" in challenging the alleged vertical nonprice agreement between NYNEX and AT&T. Pet. App. 10a. Although Discon had not cited *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959), the court held that the group boycott (or concerted refusal to deal) doctrine of *Klor's* might be "extended . . . to the situation where only a single retailer and a single manufacturer conspire." Pet. App. 11a. The court acknowledged that "such arrangements will often resemble exclusive distributorship agreements, which are generally considered permissible under the rule of reason," and that "*in general*, two-firm vertical combinations will be scrutinized as exclusive distributorship controversies, rather than as group boycotts." Pet. App. 12a. The court further recognized, relying on *Sharp*, that "[i]n the vast majority of cases, the decision to discriminate in favor of one supplier over another will have a pro-competitive intent and effect." *Id.* But the court held that no "pro-competitive rationale appears on the face of the complaint," which alleges only an "intent and effect" to "overcharge captive rate-paying customers." *Id.* Without inquiry into whether the amended complaint alleged any harm to competition (rather than to Discon) in the alleged markets for removal services, the court held: "Discon has alleged a cause of action under, at least, the rule of reason, and possibly under the *per se* rule applied to group boycotts in *Klor's*, if the restraint of trade has no purpose except stifling competition." Pet. App. 13a (internal quotation marks omitted).[11]

As to Section 2, the court of appeals quickly disposed of Discon's claims that NYNEX had monopolized and

[11] On the "pro-competitive" side of the inquiry, the court attached a footnote simply declaring that the "traditional rationale for applying the rule of reason to two-firm group boycotts—the promotion of interbrand competition over intrabrand competition—does not exist in this case." Pet. App. 13a n.6.

attempted to monopolize the alleged markets for removal services, explaining that NYNEX was not a competitor or would-be competitor in the alleged markets at all and, therefore, could not be an actual or threatened monopolist. Pet. App. 13a-14a. The court of appeals then revived Discon's Section 2 claim of conspiracy to monopolize, though on a basis it made up on its own. Discon had claimed that the conspiracy was to make *NYNEX* the monopoly provider of removal services,[12] but that theory was also subject to the fatal defect that NYNEX was not a provider of removal services at all. The Second Circuit therefore recharacterized the Section 2 conspiracy claim as alleging that NYNEX entered into an agreement with the specific intent to give *AT&T* monopoly power as a seller of removal services (to, *e.g.*, NYNEX itself). Pet. App. 15a. On that basis the court revived the Section 2 conspiracy claim along with the Section 1 conspiracy claim.

On NYNEX's petition for a writ of certiorari, this Court invited the Solicitor General to express the views of the Government. The Government declined to defend the boycott rationale of the Second Circuit, but it defended the Section 1 result under a rule-of-reason theory based on regulatory evasion as an antitrust offense and urged denial of review. SG Pet. Br. 7-12, 18-20. This Court granted certiorari on March 23, 1998. J.A. 126.

INTRODUCTION AND SUMMARY OF ARGUMENT

A buyer's freedom to replace one supplier with another is the engine prodding rival suppliers to lower cost and improve quality and, thus, is the essence of a competitive economy. The Second Circuit's decision in this case cre-

[12] *See* J.A. 111-12 (Am. Compl. ¶ 107); Discon C.A. Br. 27 (MECo and AT&T conspired and "took overt acts in concert with the specific intent to have MECO monopolize the central office removal market in New York"); Discon C.A. Reply Br. 7 ("MECO attempted to, and did, monopolize the removal market, as well as conspire to monopolize it").

ates antitrust standards under both Section 1 and Section 2 of the Sherman Act that threaten this essential freedom. By allowing a disappointed supplier to impose the burdens of costly treble-damages antitrust litigation on its former purchaser in the absence of any specific and plausible allegation of any threat to competition in the supplier markets, the decision chills efficient supplier changes and thereby harms the very competitive process the antitrust laws are designed to protect.

I. The Second Circuit improperly invoked the antitrust category of group boycott, or concerted refusal to deal, in allowing the Section 1 conspiracy claim to proceed. That invocation is plain error. A group boycott is a subspecies of horizontal agreement, *i.e.*, an agreement between rivals, and the law of boycotts reflects the distinctive antitrust concern with such combinations of direct competitors. This case involves only an alleged vertical agreement between a purchaser (NYNEX) and a supplier (AT&T), making the law of group boycotts inapplicable.

The Second Circuit was mistaken not only in its labeling but in its substance. The alleged vertical nonprice agreement cannot be subject to a *per se* standard of liability. As this Court has repeatedly made clear, including in *State Oil Co. v. Khan*, 118 S. Ct. 275, 281 (1997), *Sharp, supra,* and *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), a vertical nonprice agreement between a purchaser and its supplier typically serves wholly legitimate purposes and is therefore subject to the rule of reason, which requires a Section 1 plaintiff to make proper allegations of and to prove harm to competition. Those requirements are essential to protecting business freedom against burdensome suits by disappointed suppliers.

Contrary to the Second Circuit's suggestion, the alleged harm in the market in which NYNEX sells telephone

service does not satisfy the requirement of harm to competition. That market is not alleged in the amended complaint as a relevant market, and rightly so, for the alleged fraudulent overcharging of ratepayers is not an antitrust concern: indeed, it had nothing to do with harming any competitive activity among rival sellers of telephone services at all. The necessary inquiry is whether competition was harmed in the only relevant markets, the alleged markets for removal services sold to NYNEX and in the New York State area.

As to those markets, however, there are critically missing allegations of harm to competition, not competitors: more than harm to Discon, but harm to the range of existing and potential rival sellers of removal services marketwide, thus harming the buyers in the market (*i.e.*, telephone companies) by subjecting them to diminished output and higher prices protected by entry barriers. This void in Discon's claims cannot be discounted as mere insufficient detail. Any suggestion of entry barriers or other facts needed to imply overall market harm would be inconsistent with Discon's own pleadings. Moreover, it is inherently implausible as an economic matter to suggest, as the Second Circuit did, that NYNEX would agree to subject itself to such exploitation at the hands of sellers in a constricted market for removal services. In these circumstances, to ensure adequate protection for the vital freedom of buyers to change suppliers, the omissions of essential facts indicating harm to competition, not competitors, should be determinative and require dismissal of Discon's Section 1 claim.

II. The Second Circuit's reinstatement of Discon's claim of Section 2 conspiracy is subject to the same flaw and others. Because a conspiracy to monopolize here would be a conspiracy in restraint of trade in violation of Section 1, the failure of the allegations of Section 1 conspiracy defeats the Section 2 conspiracy claim. The little-used claim of Section 2 conspiracy should not be permit-

ted to reopen the very avenues for abusive antitrust litigation foreclosed by a proper dismissal of the Section 1 claim.

In addition, the Second Circuit erred in reviving the Section 2 claim based on its own theory that NYNEX conspired to give *AT&T* a monopoly in the markets for removal services. The conspiracy-to-monopolize claim of the amended complaint is not fairly read to make such an allegation. Rather, as Discon made explicit in the court of appeals, that claim alleges that *NYNEX* would be the monopolist, in precise parallel with the monopolization and attempted-monopolization claims. All three Section 2 claims rested on Discon's attempt to separate MECo from NYNEX, and once the Second Circuit correctly rejected that attempt, it should have dismissed the conspiracy-to-monopolize claim for the same reason it dismissed the other Section 2 claims: because NYNEX was not an actual or planned seller in the relevant markets at all (much less a would-be monopolist).

Finally, even if Discon had presented the claim formulated by the Second Circuit, the factual allegations of its amended complaint cannot fairly be held to satisfy the essential requirement for a conspiracy to monopolize claim—that the parties conspired with the specific intent to give AT&T a monopoly. The entire amended complaint rests on the theory that the specific intent of the parties to the conspiracy was for NYNEX to engage in regulatory evasion and for AT&T to share in the spoils. Since that alleged scheme does not depend on AT&T's becoming a monopoly provider of removal services, and since it would be economically irrational for NYNEX to give monopoly power to AT&T, a specific intent to create such a monopoly cannot be supported on the facts alleged in the amended complaint.

ARGUMENT

This is a case of alleged regulatory fraud masquerading as an antitrust case. P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 1644'c, at 726-28 (Supp. 1997). The alleged overcharging of ratepayers, however wrongful as a regulatory matter, is not even alleged to harm any competitive activity, any rivalry between competing sellers, in the telephone-service market. This alleged ratepayer harm therefore is simply outside the ambit of antitrust law, which does not address all wrongs against consumers or all raising of price, but only a subset arising from impairments to the process of rivalry among firms, *i.e.*, competition. The only proper focus, accordingly, is on the removal-services markets actually alleged in the amended complaint. Although Discon has alleged harm to itself in those markets, "[i]t is axiomatic that the antitrust laws were passed for 'the protection of *competition*, not *competitors*.'" *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993) (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962)). Discon has failed to meet that standard, for there are critically missing allegations of present or threatened curtailment of supply and raising of price, protected by entry barriers, through the squelching of existing and readily available competition in the alleged removal-services markets.

Under the proper legal standards requiring actual or threatened harm to marketwide competition, the district court's dismissal of both the Section 1 and Section 2 conspiracy claims was proper, and the Second Circuit's reinstatement should be reversed. Because this antitrust case, like others, has come to the Court on a motion to dismiss,[13]

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[13] *E.g.*, *Hartford Fire Ins. Co. v. California*, 509 U.S. 764 (1993); *Summit Health, Ltd. v. Pinhas*, 500 U.S. 322 (1991); *Hoover v. Ronwin*, 466 U.S. 558 (1984); *Associated General Contractors of*

the Court "must assume that the [plaintiff] can prove the facts alleged in its amended complaint." *Associated General Contractors of California, Inc. v. California State Council of Carpenters*, 459 U.S. 519, 526 (1983). "It is not, however, proper to assume that the [plaintiff] can prove facts that it has not alleged or that the defendants have violated the antitrust laws in ways that have not been alleged." *Id.* (footnote omitted, noting plaintiff's "adequate opportunity to amend its pleading"). Moreover, careful attention to what is alleged and what is not alleged is necessary to prevent the burdens and risks of litigation from undermining antitrust law's very objectives by chilling legitimate changes of suppliers and other procompetitive marketplace conduct: it is appropriate on a motion to dismiss "in a case of this magnitude . . . to insist upon some specificity in pleading before allowing a potentially massive factual controversy to proceed." *Id.* at 528 n.17.

I. THE AMENDED COMPLAINT DOES NOT STATE A VALID CLAIM OF SECTION 1 CONSPIRACY

The Second Circuit, in holding that Discon had stated a valid claim of an agreement in violation of Section 1 of the Sherman Act, invoked the antitrust category of group boycott or (its equivalent) concerted refusal to deal. The court recognized that category to encompass the possibility of either a *per se* or a rule-of-reason standard, as this Court has expressly ruled (*Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*, 472 U.S. 284, 293, 297-98 & n.9 (1985)) and as the Second Circuit had recognized in previous decisions (*Balaklaw v. Lovell*, 14 F.3d 793, 800 (2d Cir. 1994); *Capital Imaging Assoc. v. Mohawk Valley Medical Assoc., Inc.*, 996

California, Inc. v. California State Council of Carpenters, 459 U.S. 519 (1983); *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982); *St. Paul Fire & Marine Ins. Co. v. Barry*, 438 U.S. 531 (1978); *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389 (1978); *Gulf Oil Corp. v. Copp Paving Co.*, 419 U.S. 186 (1974).

F.2d 537, 543 (2d Cir.), *cert. denied*, 510 U.S. 947 (1993)).[14] In reinstating the challenge to the alleged NYNEX-AT&T agreement, the court of appeals accordingly held that the amended complaint was sufficient under one or the other standard, and it relied critically on the regulatory-evasion theory of the amended complaint in so holding. Pet. App. 10a-12a. The Second Circuit was wrong.

A. The Purely Vertical Agreement At Issue Is Not A Group Boycott

The alleged NYNEX-AT&T agreement is a purely vertical nonprice agreement between a purchaser and its supplier, as the Second Circuit acknowledged. *See* Pet. App. 10a & n.5. Nevertheless, the Second Circuit borrowed the category of group boycott, or concerted refusal to deal, from this Court's decision in *Klor's* and suggested that the category might "extend" to cover this agreement. Pet. App. 12a. That characterization is plainly incorrect. *Klor's*, as well as *United States v. General Motors Corp.*, 384 U.S. 127 (1966), and all of the other decisions of this Court falling into the familiar "group boycott" category of antitrust analysis, involved *horizontal* agreements, *i.e.*, agreements among competitors at the same level of distribution. *See Sharp*, 485 U.S. at 734 (*Klor's* and *General Motors* both "involved horizontal combinations"); ABA Section of Antitrust Law, *Antitrust Law Developments* 100-10 (4th ed. 1997).[15]

[14] *See Northwest Wholesale Stationers*, 472 U.S. at 293 (using "group boycott" and "concerted refusal to deal" interchangeably); *id.* at 297 (district court was "correct" in "recognizing that not all concerted refusals to deal should be accorded *per se* treatment"); *id.* at 297 n.9 (approving district court's application of "Rule of Reason" to "group boycott").

[15] *See, e.g., FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990); *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447 (1986); *Northwest Wholesale Stationers, supra; Klor's, supra; Northern*

It is thus a necessary condition for classification as a group boycott that a group of *competitors* be combining. In particular, they must be agreeing among themselves that they will not do business with—that they will boycott or, acting in concert, refuse to deal with—some other firm or firms. The essential precondition of a group boycott is a horizontal agreement. *See U.S. Healthcare, Inc. v. Healthsource, Inc.*, 986 F.2d 589, 594 (1st Cir. 1993) (Boudin, J.) ("a purely vertical arrangement, by which (for example) a supplier or dealer makes an agreement exclusively to supply or serve a manufacturer, is not a group boycott"); Pet. 10 n.4 (citing authorities from nine other circuits).

This precondition reflects basic antitrust policy. The reason a distinctive body of antitrust law has developed for such agreements is precisely that they involve "the aggregation of the power of several competitors—a reason that does not apply to distribution restraints involving a single manufacturer's product" or, indeed, to other vertical nonprice agreements. VIII P. Areeda, *Antitrust Law* ¶1644c, at 474 (1989) (footnote omitted); *see State Oil Co.*, 118 S. Ct. at 281 ("vertical restraints are generally more defensible than horizontal restraints"); *Arizona v. Maricopa County Medical Soc.*, 457 U.S. 332, 348 n.18 (1982). And, as this Court explicitly ruled in *Sharp*, the critical distinction between vertical and horizontal agreements cannot be erased by saying, as the Second Circuit did, that a vertical agreement might "be characterized as a horizontal restraint of trade" if it "seeks to disadvantage" one of the parties' competitors (Pet. App. 11a): such a mischaracterization confuses the *effects* of an agreement, which are inherently horizontal if they harm "competition," with the character of the agreement, which is intrinsically vertical if it is between a firm and

Pac. Ry. v. United States, 356 U.S. 1 (1958); *Fashion Originators' Guild v. FTC*, 312 U.S. 457 (1941); *Eastern States Retail Lumber Dealers' Ass'n v. United States*, 234 U.S. 600 (1914).

its supplier (or distributor). *Sharp*, 485 U.S. at 730 & n.4. The Second Circuit's invocation of the "group boycott" characterization for a vertical agreement thus was mistaken in both definitional and policy terms.

The court's mistake cannot be dismissed as an empty labeling problem. Businesses and their counsel broadly rely on established categories of antitrust doctrine to add clarity and predictability to their legal analyses of actual or contemplated marketplace conduct. Although doctrinal categories are not always neat and mutually exclusive, they define essential limits; instability and confusion are fostered, and businesses may be deterred from efficient conduct by the prospect of risky and costly treble-damages litigation, when courts breach those limits. In this case, the proper categorization dramatically changes the legal landscape. While a "group boycott" characterization would raise the uncertain prospect of *per se* analysis,[16] correctly characterizing the NYNEX-AT&T agreement as a *vertical* nonprice agreement makes clear that the agreement is subject to rule-of-reason standards, which Discon cannot meet, as explained below.

B. The Vertical Purchaser-Supplier Nonprice Agreement Here Can Be Challenged Only By Alleging And Proving Harm To Competition Under The Normal Rule Of Reason

The Second Circuit's reliance on *Klor's* allowed it to countenance the possibility of condemning the alleged

[16] The line separating group boycotts that are *per se* unlawful from those which are subject to the rule of reason has been acknowledged to be an uncertain one. *See Northwest Wholesale Stationers*, 472 U.S. at 294 ("there is more confusion about the scope and operation of the *per se* rule against group boycotts than in reference to any other aspect of the *per se* doctrine") (internal quotation marks omitted); *see also FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. at 452-53 n.9 (Brennan, J., dissenting); *St. Paul Fire & Marine Ins. Co. v. Barry*, 438 U.S. at 543; ABA Section of Antitrust Law, *Antitrust Law Developments* 101-02 (4th ed. 1997).

NYNEX-AT&T agreement without requiring proper allegations and proof of harm to competition, *i.e.*, of market-wide curtailment of output and raising of price, through impairment of the process of competition by which actual or potential rivals offer alternatives to buyers. But such requirements are essential for any proper challenge to a purchaser-supplier agreement, even in the regulated-utility setting here.

1. *Per Se Analysis Does Not Apply*

"Ordinarily, whether particular concerted action violates § 1 of the Sherman Act is determined through case-by-case application of the so-called rule of reason—that is, 'the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition.'" *Sharp*, 485 U.S. at 723 (quoting *GTE Sylvania*, 433 U.S. at 49); *see State Oil Co.*, 118 S. Ct. at 279. Certain types of agreement, however, "have such predictable and pernicious anticompetitive effect, and such limited potential for procompetitive benefit, that they are deemed unlawful *per se*." *State Oil Co.*, 118 S. Ct. at 279. Such exceptions to the usual requirements of alleging and proving anticompetitive effects have been adopted with "reluctance" (*id.*) and only when experience has shown that the particular type of agreement is "manifestly anticompetitive" because it "would always or almost always tend to restrict competition and decrease output." *Sharp*, 485 U.S. at 723-24 (internal citations and quotation marks omitted).

No *per se* standard can be applied in this case. This Court has squarely rejected the application of a *per se* standard to vertical nonprice agreements. In *GTE Sylvania*, the Court overruled *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), "thereby rejecting application of a *per se* rule in the context of vertical non-

price restrictions." *State Oil Co.*, 118 S. Ct. at 281; *see* U.S. Br. at 15, in *State Oil Co.* (under *GTE Sylvania*, "vertical non-price restraints should be judged under the rule of reason"). Subsequently, the Court not only has reiterated the requirement of rule-of-reason analysis for vertical nonprice agreements (*Sharp, supra*; *State Oil Co., supra*), but has insisted on its importance: the Court has "been solicitous to assure that the market-freeing effect of [its] decision in *GTE Sylvania* is not frustrated by related legal rules." *Sharp*, 485 U.S. at 726. *See id.* ("rules in this area should be formulated with a view towards protecting the doctrine of *GTE Sylvania*").

The reason for protecting vertical nonprice agreements against treble-damages liability in the absence of proven market harm fully applies to the agreement at issue. Even if the alleged NYNEX-AT&T agreement committed NYNEX to exclusive purchases of removal services from AT&T—which it is not alleged to do (*see* page 5, *supra*) —it would be a type of agreement that has long been recognized to serve legitimate, procompetitive objectives. Exclusive dealing arrangements often provide the buyer assurance of supply, stability of price, and savings of transaction costs, while enabling the supplier to make reliable plans for building, acquiring, or using physical resources as well as hiring employees. Such agreements, therefore, have long been protected against liability in the absence of proof of harm to competition. *See, e.g., Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 29-31 (1984); *id.* at 46 (O'Connor, J., concurring); *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 334 (1961); *Standard Oil Co. v. United States*, 337 U.S. 293, 306-07 (1949); *U.S. Healthcare, Inc.*, 986 F.2d at 595; *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 236-37 (1st Cir. 1983); *see* SG Pet. Br. 14 n.11 ("such agreements are considered to enhance efficiency"). The Second Circuit itself recognized that "[i]n the vast majority of cases, the decision to discriminate in favor of

one supplier over another will have a pro-competitive intent and effect." Pet. App. 12a. Accordingly, treble-damages liability for a vertical nonprice agreement like the alleged NYNEX-AT&T agreement cannot be imposed without the proof of harm to competition required by the rule of reason. *See Jefferson Parish*, 466 U.S. at 31 ("Without a showing of actual adverse effect on competition, [a plaintiff challenging an exclusive dealing arrangement] cannot make out a case under the antitrust laws . . . .").

2. *The Rule Of Reason, Requiring Allegations And Proof Of Harm To Competition, Applies*

This requirement is not met simply because an individual competitor has been harmed. The very meaning of this Court's repeated insistence that the Sherman Act protects "*competition*, not *competitors*" (*Brown Shoe Co.*, 370 U.S. at 320; *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977); *Brooke Group*, 509 U.S. at 224) is that an agreement, to be condemned as anticompetitive, must make purchasers in the market worse off by significantly limiting the overall range of existing as well as potential sellers, or their ability to compete, so as to subject purchasers to reduced output and raised price. In the absence of such a marketwide contraction, purchasers can turn to alternatives, whether existing sellers or new entrants, and any harm is only to competitors, not competition. *See Tampa Electric*, 365 U.S. at 327 (foreclosure of "competition" under Section 3 of the Clayton Act, 15 U.S.C. § 14, requires marketwide inquiry); *id.* at 335 (applying result to Section 1 of the Sherman Act).[17]

[17] This point is often formulated as a requirement of proof of actual or threatened market power to satisfy the anticompetitive effects test for a rule-of-reason violation. *See Digital Equipment Corp. v. Uniq Digital Technologies, Inc.*, 73 F.3d 756, 761 (7th Cir. 1997); *SCFC ILC, Inc. v. Visa USA, Inc.*, 36 F.3d 958, 965-66 (10th Cir. 1994), *cert. denied*, 515 U.S. 1152 (1995); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 229 n.11, 230 (D.C. Cir. 1986) (Bork, J.), *cert. denied*, 479 U.S. 1033 (1987); *Ball Memorial Hospital, Inc. v. Mutual Hospital Ins., Inc.*, 784 F.2d 1325, 1334-35 (7th Cir. 1986); *see also Apex Hosiery Co. v. Leader*, 310 U.S. 469, 512 (1940) (no antitrust liability for agreements that "fall short, both in their purpose and effect, of any form of market control of a commodity").

Thus, a Section 1 plaintiff challenging a purchaser-supplier nonprice agreement must prove—and, at the complaint stage, must make allegations from which reasonable inferences may be drawn—that the agreement has harmed or will harm marketwide competition to the detriment of the buyers in that market.

These preconditions for pursuing a Section 1 claim are especially important when firms change suppliers. Freedom to make such changes is the critical procompetitive mechanism by which the free market economy induces sellers to reduce their costs and improve their quality to win customers in competition with rivals, yet the termination of a supplier presents a predictable invitation for burdensome treble-damages litigation, or threats of such litigation, by a supplier wanting to make its purchaser pay a litigation price for choosing to change. Preserving the requirement of harm to competition—with appropriate insistence on specificity at the complaint stage to ensure that the heavy burdens of further proceedings are themselves adequately justified—is critical for protecting the leeway of businesses to make competitively vital decisions to change suppliers.

Accordingly, the competitive importance of freedom to replace suppliers, like the competitive importance of freedom to replace distributors, has been recognized in the large number of judicial decisions rejecting claims by disappointed suppliers under the same standard applied to terminated distributors: "a complaint which simply alleges that a manufacturer substituted one distributor for another fails to state a violation of the rule of reason, *unless* it also alleges anticompetitive effect at the interbrand

level."[18] That body of judicial experience reflects this Court's repeated insistence on "protecting the doctrine of *GTE Sylvania*." *Sharp*, 485 U.S. at 726; *see Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 763-64 (1984). Any relaxation of the requirements that the plaintiff fully bear the burden of alleging and proving marketwide harm in this context would threaten the very result condemned by this Court in *Sharp*: "Manufacturers would be likely to forgo legitimate and competitively useful conduct rather than risk treble damages and perhaps even criminal penalties." 485 U.S. at 728.[19]

At the petition stage, the Government read the Second Circuit opinion as relaxing the plaintiff's requirements and instead shifting to the defendants some burden to produce and defend a "valid procompetitive justification" for the

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[18] *Crane & Shovel Sales Corp. v. Bucyrus-Erie Co.*, 854 F.2d 802, 806 (6th Cir. 1988); *see, e.g., Coastal Transfer Co. v. Toyota Motor Sales, U.S.A.*, 833 F.2d 208, 211 (9th Cir. 1987) ("recurrent case of the jilted . . . supplier who loses a manufacturer's franchise and accuses the manufacturer and the new suitor of attempting to monopolize something"); *Rutman Wine Co. v. E. & J. Gallo Winery*, 829 F.2d 729, 735 (9th Cir. 1987); *Great Escape, Inc. v. Union City Body Co.*, 791 F.2d 532, 539 (7th Cir. 1986); *Dunn & Mavis, Inc. v. Nu-Car Driveaway, Inc.*, 691 F.2d 241, 245 (6th Cir. 1982); *A.H. Cox & Co. v. Star Machinery Co.*, 653 F.2d 1302, 1306 (9th Cir. 1981) (Kennedy, J.); *Burdett Sound, Inc. v. Altec Corp.*, 515 F.2d 1245, 1249 (5th Cir. 1975).

[19] Because freedom to change suppliers is so vital to a competitive economy, the harmful effect of lowering the threshold for extensive and uncertain antitrust suits by disappointed suppliers is akin to that of weakening the standards for challenging pricing behavior—as to which the Court has noted: "[M]istaken inferences in cases such as this one are especially costly, because they chill the very conduct the antitrust laws are designed to protect. '[W]e must be concerned lest a rule or precedent that authorizes a search for a particular type of undesirable pricing behavior end up by discouraging legitimate price competition.'" *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986) (citation to *Monsanto* omitted; quoting *Barry Wright*, 724 F.2d at 234).

challenged vertical nonprice agreement. SG Pet. Br. 12-13, 16-17. But any such standard, by forcing businesses to justify their choices to government enforcers and courts in the absence of present or threatened marketwide harm, would substantially increase litigation costs and thus have the very adverse effect on market freedom that this Court and lower courts have strived to prevent. Not surprisingly, then, the suggestion violates well-established black-letter law: "The plaintiff bears the burden of proving that a restraint has a substantial anticompetitive effect. Absent such an anticompetitive effect, the defendant need not proffer justifications for its conduct." ABA Section of Antitrust Law, *Antitrust Law Developments* 55 (4th ed. 1997) (footnotes citing decisions omitted).

No precedent supports watering down the fundamental rule-of-reason requirement of alleging and proving market harm to challenge a vertical nonprice agreement. The two decisions cited by the Government provide no such support. *See* SG Pet. Br. 16 (citing *FTC v. Indiana Federation of Dentists*, 476 U.S. 447 (1986), and *NCAA v. Board of Regents*, 468 U.S. 85 (1984)). Both involved *horizontal* agreements—one between colleges competing to attract television money for their sporting events (*NCAA*), the other between dentists competing for the dollars paid by patients and their insurance carriers (*Indiana Federation*)—that directly limited the parties' competition with one another on important price or service terms. Even for such a horizontal agreement, which the Court in *NCAA* described as involving a "naked restraint on price and output" (468 U.S. at 110) that might have been condemned as *per se* unlawful in the absence of special factors (the sports and professional-association contexts), the Court did not dispense with the requirement of market harm. Instead, it concluded that the requirement was satisfied without "elaborate market analysis" (*Indiana Federation*, 476 U.S. at 461) based on the factfinder's findings of

" 'actual detrimental effects, such as reduction of output.' " *Id.* at 460; *NCAA*, 468 U.S. at 109-10.[20]

Thus, even for horizontal agreements not covered by *per se* rules, this Court's decisions require plaintiffs to allege and prove market harm.[21] But whatever may ultimately be determined for certain horizontal agreements, no weakening of plaintiffs' proof requirements could apply to vertical nonprice agreements after *GTE Sylvania* and *Sharp*. *See U.S. Healthcare, Inc.*, 986 F.2d at 594-95 (rejecting "quick look" analysis of vertical exclusive dealing arrangements). No such approach could be squared with this Court's insistence on maintaining the line between horizontal and vertical agreements with clarity so as to preserve firms' important freedom to choose, to change, and to enter into exclusive-dealing and similar contracts with suppliers. *See Sharp*, 485 U.S. at 726, 730 & n.4. Proper allegation and proof of marketwide harm must remain a precondition to a Section 1 challenge to a vertical nonprice agreement.

3. *The Regulated Setting Does Not Weaken The Requirements*

The regulated monopoly setting alleged in the present case provides no justification for weakening the basic rule-

[20] In *National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978), the Court noted that "no elaborate industry analysis is required to demonstrate the anticompetitive character" of an agreement among 69,000 engineers nationwide to refuse to discuss price with customers until after selection of the engineer. Not surprisingly, this point was not in dispute before this Court, which instead was presented with the issue whether the agreement could be justified by considerations of safety and professional ethics.

[21] Even in the horizontal context, the suggestion of a "quick look" or "stepwise" approach, shifting a burden of justification to the private parties to an agreement that is not unlawful *per se*, has been criticized. *See* Kolasky, "The Department of Justice's 'Stepwise' Approach Imposes Too Heavy a Burden on Parties to Horizontal Agreements," *Antitrust* at 41 (Spring 1998).

of-reason requirements for challenging such purchaser-supplier contracts. Regulated companies (or, more generally, businesses operating under cost-plus contracts) are no less in need of the freedom to make efficient changes of suppliers, or to enter into efficiency-enhancing requirements contracts, than are other companies. That freedom, and its procompetitive benefits, would be threatened by diluting the critical requirement of market harm for a disappointed supplier to maintain a Section 1 challenge. As the Government recognized at the petition stage, "[v]irtually any requirements contract could be characterized as a 'two-firm vertical' agreement 'to discriminate in favor of one supplier over another.' " SG Pet. Br. 14 n.11 (quoting Pet. App. 12a).

Indeed, the regulated utility setting alleged here provides, if anything, particular reasons to strengthen, not weaken, the pleading and proof requirements. With regulators monitoring the very sort of conduct alleged in the amended complaint (*see* Pet. App. 5a; note 7, *supra*), "strict antitrust scrutiny is less likely to be necessary." *Kartell v. Blue Shield of Massachusetts, Inc.*, 749 F.2d 922, 931 (1st Cir. 1984), *cert. denied*, 471 U.S. 1029 (1985). At the same time, under Discon's premise of pass-through of excess costs to captive telephone ratepayers, downstream consumers could less easily avoid the predictable increase in supplier costs that the threat of burdensome antitrust litigation would impose on a regulated firm like NYNEX. It is perverse to deter efficient input choices precisely where the adverse impact on consumers, under Discon's theory, would be least escapable.

C. The Allegations Of Fraudulent Overcharging Of Telephone Ratepayers Do Not State A Competitive Harm

In invoking group-boycott doctrine and suggesting *per se* condemnation, the Second Circuit relied on the claim

of regulatory evasion as itself establishing competitive harm. That reliance fundamentally confused the purported harm to ratepayers in the regulated telephone-service market, which is only a regulatory problem, with the required harm to competition in the alleged markets for removal services, the only markets where competition is even claimed to be restrained. The ruling rests on two important errors.

1. The Second Circuit violated the elementary requirement that relevant markets be defined. The effect on "competition, not competitors," cannot be assessed without specifying the relevant markets, which determine the range of existing and potential rivals available to purchasers. *See Tampa Electric*, 365 U.S. at 327, 329 ("the threatened foreclosure of competition must be in relation to the market affected"; "the relevant market is the prime factor in relation to which the ultimate question, whether the contract forecloses competition in a substantial share of the line of commerce involved, must be decided"); *see Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456 (1993) (" '[w]ithout a definition of [the relevant] market there is no way to measure [the defendant's] ability to lessen or destroy competition' "); *GTE Sylvania*, 433 U.S. at 53 n.21 ("an antitrust policy divorced from market considerations would lack any objective benchmarks").[22] Accordingly, it is well settled that " '[w]ithout defining the relevant market, there is no meaningful context within which to assess the restraint's com-

[22] Contrary to the Government's suggestion at the petition stage, *Jefferson Parish* did not repudiate the need for careful attention to the market where competition is allegedly restrained. *See* SG Pet. Br. 9 (describing *Jefferson Parish*, 466 U.S. at 29-30, as recognizing the availability of liability for a "restraint in one market that causes anticompetitive effects in another market"). The cited passage indicates nothing more remarkable than that absolute precision in defining the exact contours of the relevant market may not be needed where the challenged agreement could not be found to constrain overall market competition under any of the possible market definitions. 466 U.S. at 29-31.

petitive effects." ABA Section of Antitrust Law, *Antitrust Law Developments* 59 (4th ed. 1997) (citing *Copperweld*, 467 U.S. at 768; *Arnold, Schwinn & Co.*, 388 U.S. at 381-82; *Times-Picayune Pub. Co. v. United States*, 345 U.S. 594, 615 (1953); *United States v. Columbia Steel Co.*, 334 U.S. 495, 519 (1948)); *see DeVoto v. Pacific Fidelity Life Insurance Co.*, 618 F.2d 1340, 1345 (9th Cir. 1980) (Kennedy, J.) ("Absent per se violation, competitive injuries must be defined in terms of a discrete market.").[23] By ignoring this principle, the Second Circuit failed even to ask whether *competition* was harmed in any market here, let alone in the alleged markets.

2. That failure in turn led the court to misidentify the alleged problem in the telephone-service market as a competitive problem. Wrongs such as fraud, whether directed to consumers or rivals, do not constitute an antitrust violation in the absence of proof of the required adverse effect on market competition. This Court often has recognized that the antitrust laws, which supplemented (and did not subsume) the preexisting and distinct bodies of law on fraud and unfair competition (and even common-carrier regulation), "do not create a federal law of unfair competition or 'purport to afford remedies for all torts committed by or against persons engaged in interstate commerce.' " *Brooke Group*, 509 U.S. at 225 (quoting *Hunt v. Crumboch*, 325 U.S. 821, 826 (1945)); *see City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 378-79

[23] Inattention to the relevant market undermines the assessment not only of any claims of harm to competition but also of antitrust standing and injury. For example, except for its now-dismissed claim as a ratepayer, Discon's only relationship to the market for telephone services was not as a consumer or competitor, but as a supplier to the sellers. Suppliers in that position have generally been barred from suing. *See SAS of Puerto Rico, Inc. v. Puerto Rico Telephone Co.*, 48 F.3d 39, 42, 44 (1st Cir. 1995) (citing II P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 375 (rev. ed. 1995)); *see also Associated General Contractors*, 459 U.S. at 539.

(1991) (antitrust laws do not provide remedy for political corruption); *Apex Hosiery*, 310 U.S. at 512 ("the Sherman Act was not enacted . . . to afford a remedy for wrongs, which are actionable under state law, and result from combinations and conspiracies which fall short, both in their purpose and effect, of any form of market control of a commodity"); *see Sitkin Smelting & Ref. Co. v. FMC Corp.*, 575 F.2d 440, 448 (3d Cir.) ("the Sherman Act may not be extended beyond its intended scope and used to police the morals of the marketplace"), *cert. denied*, 439 U.S. 866 (1978). The Second Circuit's reliance on regulatory evasion in this case disregards that principle: it transforms into an antitrust problem what is at most an alleged fraud on regulators acting as a surrogate for consumers under a distinct body of law.

At the petition stage, the Government elaborated the Second Circuit's reliance on the alleged regulatory evasion as causing anticompetitive effects into a full-fledged theory of antitrust liability. SG Pet. Br. 7-12. According to the Government: "[a]n agreement between a regulated monopolist and its supplier to exclude a competing supplier from the market, when that agreement has the purpose and effect of enabling the monopolist to evade regulatory scrutiny and exercise market power in a downstream market, violates Section 1 in the absence of any procompetitive justification." *Id.* at 12. By its terms, this standard dispenses with any requirement of harm to competition in the market from which the supplier was allegedly excluded. The Government's striking proposal, like the Second Circuit reference it elaborates, is insupportable.

To begin with, the amended complaint does not identify any telephone-service market (where NYNEX sold service) as a relevant market in which competition was restrained. Rather, the only relevant markets in which competition was allegedly restrained are two markets for removal services sold by Discon—one where NYNEX

was the sole buyer ("at NYT") and the other where NYNEX was the dominant buyer ("in the New York State area"). *See* pages 3-4, *supra*. That definition of the relevant markets reflects the simple fact that the alleged regulatory-evasion scheme had nothing to do with keeping out any rival sellers of telephone service.

More importantly, the theory that mere overcharges in the regulated telephone-service market are legally sufficient to constitute anticompetitive effects supporting antitrust liability is deeply and perilously wrong. The theory rests squarely on the premise that "[a]n increase in consumer prices resulting from the exercise of market power is an anticompetitive effect." SG Pet. Br. 8; *id.* at 9 n.6 ("[t]he anticompetitive effect . . . is the *exercise* of market power"). This premise embodies a fundamental logical mistake. It starts with this Court's insistence on harm to competition, not merely competitors; it properly understands that harm to competition requires consumer exploitation through reduction of output and raising of price; but it then mistakenly transforms that concept from a *necessary* condition into a *sufficient* condition, thus bringing all reductions of output and raising of price into antitrust's fold. But while harm to competitors is not enough to constitute harm to competition, it is a precondition. The contrary assertion is a radical and deeply misconceived effort to extend antitrust law, which is concerned only with consumer harms brought about *through diminished competition*, to other forms of alleged consumer exploitation, such as fraud and regulatory evasion, that have nothing to do with impaired competition.

This Court has made clear that "the sole aim of antitrust legislation is to protect competition." *Gordon v. New York Stock Exchange, Inc.*, 422 U.S. 659, 689 (1975). The Sherman Act addresses only harms to "competitive conditions." *National Society of Professional Engineers*, 435 U.S. at 688, 690. The Act thus targets only "actions that harm the competitive process." *Clamp-All*

Corp. v. Cast Iron Soil Pipe Institute, 851 F.2d 478, 486 (1st Cir. 1988), *cert. denied*, 488 U.S. 1007 (1989); *Interface Group, Inc. v. Massachusetts Port Authority*, 816 F.2d 9, 10 (1st Cir. 1987). In this crucial respect, "the antitrust laws differ from classical regulation both in their aims and in their methods," for, unlike direct regulation, they "seek to create or maintain the *conditions* of a competitive marketplace rather than replicate the *results* of competition or correct for the defects of competitive markets." S. Breyer, *Regulation and Its Reform* 156-57 (1982); *see also Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 22 (1st Cir. 1990), *cert. denied*, 499 U.S. 931 (1991).

Given the focus of antitrust policy on the opportunities of rivals, numerous courts have recognized that the exercise of market power is *not* anticompetitive. *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 294 (2d Cir. 1979) ("[s]etting a high price may be a use of monopoly power, but *it is not in itself anticompetitive*") (emphasis added), *cert. denied*, 444 U.S. 1093 (1980).[24] Over-

[24] *See Blue Cross & Blue Shield United of Wisconsin v. Marshfield Clinic*, 65 F.3d 1406, 1412-13 (7th Cir. 1995) (Posner, C.J.) ("[T]he antitrust laws do not regulate the prices of natural monopolists. A natural monopolist that acquired and maintained its monopoly without excluding competitors by improper means . . . can therefore charge any price that it wants, for the antitrust laws are not a price-control statute or a public-utility or common-carrier rate-regulation statute.") (citations omitted), *cert. denied*, 116 S. Ct. 1288 (1996); *Alaska Airlines, Inc. v. United Airlines, Inc.*, 948 F.2d 536, 548-49 (9th Cir. 1991) (same point as *Berkey*), *cert. denied*, 503 U.S. 977 (1992); *Williamsburg Wax Museum, Inc. v. Historic Figures, Inc.*, 810 F.2d 243, 252 (D.C. Cir. 1987) ("imposition of a high price is not, in and of itself, an anticompetitive act"); *Kartell*, 749 F.2d at 927 ("Ordinarily, however, even a monopolist is free to exploit whatever market power it may possess when that exploitation takes the form of charging uncompetitive prices."); *Trace X Chem., Inc. v. Canadian Indus., Ltd.*, 738 F.2d 261, 268 (8th Cir. 1984) ("[S]etting a high price is not in itself anti-competitive."), *cert. denied*, 469 U.S. 1160 (1985).

charging consumers by exercising market power may present a regulatory problem, but it is not an antitrust problem absent impairment of rivals' opportunities. To the contrary, "the charging of a high price is, so far as potential competitors are concerned, an attracting rather than an excluding practice." *Marshfield Clinic*, 65 F.3d at 1413; *see Berkey*, 603 F.2d at 294. *See* III P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 720a, at 206 (rev. ed. 1996) ("[A] monopolist does not impair the opportunities of rivals or otherwise exclude competition by charging a monopoly price. On the contrary, high prices encourage the entry and expansion of rivals."); *id.* ¶ 720b, at 208 ("The goal of antitrust should always be to encourage *competition*, not the indefinite perpetuation of price-regulated monopoly.").

The Government itself previously recognized that antitrust law reaches evasion of rate regulation only where competition in an unregulated market is harmed. The Government told the D.C. Circuit in the Bell System litigation that regulatory evasion through cost-shifting from a competitive market to a regulated one is not a *competitive* concern unless it also results in the threat of market power in the unregulated market: it sharply distinguished regulatory evasion "that does not afford any possibility of creating market power and that raises no competitive concern" from regulatory evasion that leads to "market power in the unregulated market" and thus raises antitrust concerns.[25] That position, rather than the

[25] "Avoiding such overcharges to ratepayers in the regulated monopoly market is a regulatory concern. Under some circumstances, cross-subsidization through cost misallocation can also be a competitive concern because a firm that can recover some of the costs of its competitive operations in the rate-regulated monopoly market by including those costs in the rate base can price below cost in the competitive market without losing money. If as a result of this cross-subsidization the monopolist succeeds in driving out its competitors and preventing new entry, it may be in a position to

Government's new position, accords with the analysis of the leading commentary. *See* IIIA P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 787b, at 284-85 (1996) (antitrust law is implicated by regulated firm's activity in related market only when "the conduct really threatens the competitive vigor of a vertically or collaterally related market"; "fact that the utility is transferring monopoly profits from regulated electricity to unregulated coal [through regulatory evasion] presents no antitrust issues but simply those of appropriate regulatory review of a firm's rates"—unless conduct "effectively forecloses a large, otherwise competitive market"); *id.* ¶ 787c1, at 294 (when utility engages in rate-regulation avoidance, "antitrust is not concerned with rates as such," but "it becomes concerned when the utility's attempt to enlarge profits eliminates competition in a collateral market capable of being competitive").

Simple practical reasons underscore the importance of continuing to respect the dividing line between regulatory problems and antitrust problems. Under the Government's theory, any change of supplier by a regulated monopolist (or, perhaps, any cost-plus business), at least any change to a superficially more costly supplier, could give rise to a Section 1 claim by the displaced supplier, requiring the regulated firm to establish a procompetitive justification in costly litigation over intent and effect, thus deterring efficient changes of supplier. If suppliers could sue based on harm connected to overcharges, many of the numerous other complaints of regulatory violations made each year might also give rise to antitrust cases. Judges and juries would become embroiled in making decisions about complex and evolving regulatory accounting and pricing issues —and perhaps become entangled with regulatory agencies

raise its prices to the detriment of consumers in the unregulated market." U.S. Br. 29, *United States v. Western Elec. Co.*, No. 87-5388 (D.C. Cir. Apr. 17, 1989).

themselves, whether through attempting to coordinate with them or through simple second-guessing of key regulatory determinations—in unfamiliar, unnecessary, and inappropriate ways. *Cf. Town of Concord*, 915 F.2d at 25-29; *Kartell*, 749 F.3d at 927. However unavoidable such inquiries might be in some circumstances, this Court should reject the proposed distortion of antitrust law that would invite such difficulties here, as it rejected the Government's related attempt to blur the line between antitrust law and another regulatory regime in *Brown v. Pro Football, Inc.*, 518 U.S. 231, 236-37 (1996).[26] *See* III P. Areeda, *Antitrust Law* ¶ 720b, at 207-08 (rev. ed. 1996) (antitrust courts have avoided price regulation because "judicial tribunals lack both the expertise and the narrow jurisdictional focus necessary to make such regulatory schemes work"); IX P. Areeda, *Antitrust Law* ¶ 1712d, at 142 (1991) (Antitrust tribunals "are no better able than the regulatory authorities to examine a particular evasion. If the regulators choose not to reach it, they have introduced some indirect flexibility in their regime. If they cannot reach it, then the underlying legislation or appropriations has created such flexibility, perhaps consciously as wise public policy or as a political compromise in the enactment.").

The effort to extend antitrust law to cover regulatory evasions without anticompetitive effects is not supported by *Jefferson Parish*, the Government's only cited authority. The majority in that case and the four Justices in concurrence both observed that regulatory evasion may explain why certain tying arrangements are undertaken

[26] "We recognize, as the Government suggests, that, in principle, antitrust courts might themselves try to evaluate particular kinds of employer understandings, finding them 'reasonable' (hence lawful) where justified by collective-bargaining necessity. But any such evaluation means a web of detailed rules spun by many different nonexpert antitrust judges and juries, not a set of labor rules enforced by a single expert administrative body, namely, the [National Labor Relations] Board." 518 U.S. at 236-37.

(466 U.S. at 13 n.19, 36 n.4), but neither opinion says that the exercise of lawfully possessed market power is an "anticompetitive" effect in the absence of impairment of rivals' opportunities to compete in the market allegedly restrained. *See* IX P. Areeda, *Antitrust Law* ¶ 1712d, at 143 (1991) (discussing references to regulatory evasion in *Jefferson Parish*, explaining that the courts have not treated and should not treat "evasion of state or federal maximum price control" as counting "for or against ties, either generally or in particular cases"). Moreover, the decision cannot imply any such holding, because the case unmistakably involved alleged consumer harm *through impaired competition* (for anesthesiology services and for doctor-hospital affiliations).

In sum, transforming regulatory evasion into a Section 1 theory based on harm in the telephone-service market indefensibly and dangerously confuses a regulatory problem with an antitrust problem. The leading commentary makes this point, criticizing the Second Circuit decision for "effectively turn[ing] a claim of fraud into an antitrust claim. For example, any seller under a cost-plus contract might secretly conspire with a supplier to provide goods at inflated costs, paying a secret rebate to the seller, and with the effect of excluding alternative suppliers. As in any case of fraud or misrepresentation, the result will be that the contracted-for good is more costly and consumers are injured. But no antitrust violation is apparent unless this activity threatens monopoly in a properly defined relevant market." P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 1644'c, at 727 (Supp. 1997). Competitive analysis thus must focus not on telephone-service markets but only on the alleged markets for removal services.

D. Harm To Competition In The Removal-Services Markets Is Not Adequately Alleged

As confirmed by the Second Circuit's and Government's resort to novel efforts to transform regulatory evasion into

an antitrust problem, the amended complaint does not adequately allege harm to competition, as opposed to harm to Discon itself, in the removal-services markets actually alleged in the amended complaint. Discon has claimed that it was injured by the alleged NYNEX-AT&T agreement to exclude it from being a supplier to NYNEX, although that single buyer's change of supplier did nothing to prevent Discon from serving other available buyers of removal services. But even under Discon's artificial market definitions (removal services "at NYT" and "in the New York State area"), this alleged harm to an individual competitor does not constitute harm to competition, *i.e.*, a marketwide limitation on the ability of existing and potential suppliers of removal services to offer lower prices or better service to meet consumer demand in competition with AT&T and other providers of removal services. The amended complaint simply lacks the essential additional allegations of such market harm that should be required before allowing extensive litigation to proceed.

The amended complaint does not allege that other competitors in the removal-services markets were excluded, that purchasers as a whole in those markets were deprived of existing or easily available alternatives, or that any significant entry barriers existed to impede new firms from coming into the market to correct any shortage of output or raising of price. *See* SG Pet. Br. 9 n.8. These omissions are critical as a substantive matter; they cannot be excused as a matter of mere insufficient detail. Discon's amended complaint and original complaint show that other present and potential suppliers of removal services did exist (J.A. 111 (Am. Compl. ¶ 107)); that telephone companies can serve their removal-services needs simply by using their own employees to do this work (J.A. 83 (Am. Compl. ¶ 27)); and that entry into this business of dismantling and disposing of telephone central office equipment, far from requiring substantial sunk costs or other up-front investments, is extremely easy: Discon

immediately won a $500,000 contract and had 25 employees (with plans to triple that number) within six months (J.A. 15, 17 (Compl. ¶¶ 50, 52, 61)); J.A. 87 (Am. Compl. ¶ 40)). With such facts conceded, the omissions from the amended complaint of key allegations needed to imply marketwide harm are critical.

The determinative character of what is missing from the amended complaint is properly judged in light of the nature of the scheme alleged. For the alleged NYNEX-AT&T agreement to produce marketwide harm in the alleged removal-services markets, NYNEX would have to be agreeing to subject itself to exploitation through higher prices set by removal-services sellers in an output-constricted (and entry-protected) market. Such a claim is inconsistent with Discon's concessions about NYNEX's ability to use its own employees to remove equipment and about ease of entry into the business, as well as with Discon's allegation that NYNEX itself "effectively controlled the price at which contracts for removal services were obtained." J.A. 111 (Am. Compl. ¶ 104).

Equally important, such a claim is unsupported by the basic theory of Discon's case. The alleged profit-making mechanism of regulatory evasion in no way depended on or implied any reduction in NYNEX's own purchases of removal services, let alone a contraction of supply or raising of price of removal services marketwide. That alleged scheme produced its alleged benefits for NYNEX without any impairment of NYNEX's retention of full ability to buy removal services at competitive prices whenever it wished, whether from existing suppliers, readily available new entrants, or its own employees. Indeed, it is simply not rational economic behavior for a buyer like NYNEX to agree to create market conditions—a shortage of suppliers protected by entry barriers—in which it could then be exploited. *See Car Carriers, Inc. v. Ford Motor Co.*, 745 F.2d 1101, 1109, 1110 (7th Cir. 1984) (dismissing complaint, explaining that theory of buyer's agreement to give seller market power to exploit it is "inherently implausible," even "preposterous"), *cert. denied*, 470 U.S. 1054 (1985); *Adaptive Power Solutions, LLC v. Hughes Missile Systems Co.*, 1998 WL 172774, at *5-*6 (9th Cir. Apr. 15, 1998) (lack of "economic sense" of similar claim supports summary judgment); *Coastal Transfer*, 833 F.2d at 211 ("illogical" nature of similar claim supports summary judgment); *TV Communications Network, Inc. v. Turner Network Television, Inc.*, 964 F.2d 1022, 1026-27 (10th Cir) (dismissing similar claim of Section 2 conspiracy as "implausible"), *cert. denied*, 506 U.S. 999 (1992).

This is precisely the type of situation where, as this Court held in *Associated General Contractors*, 459 U.S. at 526, 528 n.17, an amended complaint is properly dismissed, and extensive litigation avoided, for lack of essential specificity. In the summary judgment context, this Court has barred antitrust claims that are "implausible" and "make[] no economic sense." *Matsushita*, 475 U.S. at 587. While the present case involves a motion to dismiss under Rule 12(b)(6), the required judgment whether an amended complaint is specific enough can be made only in light of the inherent economic plausibility of the plaintiff's theory of antitrust harm. In particular, given the serious burdens of litigating an antitrust case even to the summary-judgment stage, disregarding the omission of essential allegations so as to authorize proceeding on an economically implausible complaint would undermine the policy of protecting the important leeway for vertical non-price agreements recognized in *GTE Sylvania*, *Monsanto*, and *Sharp*. The amended complaint was properly dismissed by the district court.

II. THE AMENDED COMPLAINT DOES NOT STATE A VALID CLAIM OF SECTION 2 CONSPIRACY

Discon's Section 2 conspiracy-to-monopolize claim is a concerted-action Section 1 claim in a different guise. The Second Circuit's revival of this claim produces the same

practical litigation risks and burdens for vertical nonprice agreements involving changes of supplier, and thus the same economically harmful effects, as the revival of the Section 1 claim. For the same and additional reasons, the Section 2 conspiracy claim is as defective as the Section 1 claim.

1. Dismissal of the Section 2 conspiracy claim follows *a fortiori* from dismissal of the Section 1 conspiracy claim. Explaining the fact that this "curious" part of Section 2 has been so little used since its enactment one hundred years ago, but instead typically has been treated as "no more than an afterthought appended to § 1 claims," the leading commentary has observed that "[a]ny arrangement that could be considered a 'conspiracy' to monopolize must necessarily also be an unreasonable 'contract,' 'combination,' or 'conspiracy' in restraint of trade." IIIA P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 809, at 370-371 (1996); *see also* R. Posner, *Antitrust Law: An Economic Perspective* 216 (1978). At least in a private lawsuit necessarily complaining of antitrust injury, a Section 2 conspiracy must be a subcategory of a conspiracy to restrain trade.[27] The full argument made above for why the Section 1 conspiracy claim cannot survive, therefore, is also made for and *a fortiori* defeats the Section 2 conspiracy claim. If, as argued above, there is no actionable conspiracy to restrain trade, there cannot be a conspiracy to monopolize.

2. The only basis on which the Second Circuit revived Discon's Section 2 conspiracy claim was its characterization of the claim as alleging that NYNEX conspired to

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[27] Because this is a private suit requiring proof of antitrust injury, the Court need not consider here whether, for example, a conspiracy to monopolize might be proscribed in a criminal proceeding where there is no actual or threatened effect on competition in any market, but a pure intentional agreement to monopolize without any probability of success.

give *AT&T* monopoly power over removal services. Pet. App. 15a. But "[t]he Complaint, fairly read, does not include such [a] claim[]." *Ohio Forestry Ass'n, Inc. v. Sierra Club*, No. 97-16 (May 18, 1998), slip op. 11. First, the Section 2 conspiracy count parallels the immediately preceding Section 2 monopolization and attempted-monopolization counts, both of which allege that the actual or putative monopolist in the removal-services markets was NYNEX, not AT&T. *See* J.A. 110-12 (Am. Compl. ¶¶ 100, 104, 107). Second, Discon unmistakably told the Second Circuit that its Section 2 conspiracy allegation was that the conspiracy was to make NYNEX the monopolist. *See* note 12, *supra*. Third, the Second Circuit's recharacterization of the Section 2 conspiracy claim results in an economically senseless theory: that NYNEX, along with several non-AT&T providers of removal services, conspired to give AT&T monopoly power in removal-services markets where NYNEX would then be subject to exploitation as a buyer. *See* pages 38-39, *supra*. In these circumstances, the Second Circuit's *sua sponte* replacement of Discon's legally incorrect theory about NYNEX as a putative monopolist with an unpleaded and economically implausible theory about AT&T as the putative monopolist was improper. *Cf. Trest v. Cain*, 118 S. Ct. 478, 481 (1997) (noting dangers of springing such surprises on the parties).

Thus, the only Section 2 conspiracy claim that Discon can fairly be said to have made is that a monopoly by NYNEX was the object of the conspiracy. That claim, however, was subject to dismissal for the same reason the Second Circuit upheld dismissal of the claims of monopolization and attempted monopolization. NYNEX could never be a monopolist in a market where it was not, and had no plans to become, a seller at all. *See* Pet. App. 13a-14a.

3. The Second Circuit's theory, even aside from the fact that it cannot fairly be read into Discon's amended

complaint, is inadequate to sustain the Section 2 conspiracy claim. The Second Circuit recognized, as this Court has indicated and the lower courts have repeatedly held, that a Section 2 conspiracy requires that the parties conspire with the specific intent to monopolize. *See* Pet. App. 14a; *American Tobacco Co. v. United States*, 328 U.S. 781, 788-89, 809 (1946); ABA Section of Antitrust Law, *Antitrust Law Developments* 302 (4th ed. 1997). The sufficiency of Discon's conspiracy allegations under Section 2 should be judged in the light of the same protective policy against inferring conspiracies in the Section 1 context (*see Sharp, supra*; *Matsushita, supra*; *Monsanto, supra*), for the dangers that efficient marketplace conduct will be deterred by burdensome litigation are comparable.

Here, the bare-bones allegation of a conspiracy with the specific intent to monopolize should not suffice to launch extensive litigation, for much the same reasons the amended complaint does not suffice to allege marketwide harm under Section 1. As already explained, the theory that NYNEX conspired with the specific intent to subject itself, as buyer, to the monopoly power of AT&T is intrinsically implausible and inconsistent with facts conceded by Discon. At the same time, the amended complaint presents an alternative explanation for the agreement—regulatory evasion resulting in profits shared between NYNEX and AT&T—that does not in any way depend on the implausible theory of monopoly power. In these circumstances, the Section 2 conspiracy claim should be dismissed along with the Section 1 conspiracy claim. *See TV Communications Network*, 964 F.2d at 1026-27 (dismissing conspiracy-to-monopolize claim where implausibility of economic theory undermined "inference of specific intent to conspire to achieve the stated goal of the conspiracy," citing *Matsushita*, 475 U.S. at 597).

CONCLUSION

The judgment of the court of appeals should be reversed, and the district court's judgment of dismissal reinstated.

Respectfully submitted.

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June 1, 1998